

ASSEMBLY BILL

No. 1967

Introduced by Assembly Member Torrico

February 14, 2008

An act to amend Section 16642 of, and to add Section 7513.8 to, the Government Code, relating to investments.

LEGISLATIVE COUNSEL'S DIGEST

AB 1967, as introduced, Torrico. Public employee retirement: investments: sovereign wealth funds.

The California Constitution provides that the Legislature may by statute prohibit retirement board investments if it is in the public interest to do so, and providing that the prohibition satisfies specified fiduciary standards. Existing law prohibits the Public Employees' Retirement System and the State Teachers' Retirement System from investing public employee retirement funds in a company with active business operations in Sudan and in Iran, as specified.

This bill would enact the Responsible Private Equity Investment Act of 2008. The bill would prohibit the Public Employees' Retirement System (PERS) and the State Teachers' Retirement System (STRS) from investing in a private equity company that is owned in whole or in part by a sovereign wealth fund, as defined, or in a fund managed directly or indirectly by a private equity company that is owned in whole or in part by a sovereign wealth fund, if any country or federation of countries with which the sovereign wealth fund is affiliated, either directly or indirectly, is not a signatory or party to at least 5 of 6 specified international treaties. The bill would provide that this prohibition may be suspended based on information in specified human rights reports made by United States Department of State or based on

the lack of such a report, as specified. The bill would require PERS and STRS to make certain evaluations before making any additional or new investment, or renewing any existing investment, in these companies and funds, and to issue a detailed written report in connection with the evaluations. The bill would require these reports to be publicly available and available on the Internet at least 60 days prior to any final investment decision, as specified. The bill would prohibit PERS and STRS from investing in these companies and funds in certain instances, based on the evaluations, unless the board determines that the failure to do so would be inconsistent with its constitutional fiduciary responsibilities, and would require written statements regarding various investment decisions.

This bill would require PERS and STRS, on or before January 1, 2010, and every year thereafter, to file reports with the Legislature on investment decisions. The bill would specify that PERS or STRS is not required to take any action unless the board of administration of the system determines, in good faith, that the action is consistent with their constitutional fiduciary responsibilities.

This bill would indemnify from the General Fund and hold harmless the present, former, and future board members, officers, and employees of, and investment managers under contract with, these retirement systems in connection with any evaluation, report, or investment decision made in compliance with the above provisions.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

- 1 SECTION 1. The Legislature finds and declares as follows:
- 2 (a) Current members of Congress, the Chair of the Securities
- 3 and Exchange Commission, other current and former executive
- 4 branch officials, and numerous experts have expressed concern
- 5 that the growing size and influence of sovereign wealth funds could
- 6 impede regulatory enforcement, lead to increased public corruption,
- 7 and pose a threat to national security.
- 8 (b) Sovereign wealth funds are also significantly less transparent
- 9 than other investors and are much more likely to invest in order
- 10 to achieve political rather than profit-maximizing goals, increasing
- 11 the risk of financial instability.

1 (c) Many sovereign wealth funds are affiliated with, and earn
2 profits for, governing regimes with human rights records that are
3 among the worst in the world. Three of the largest sovereign wealth
4 funds, which together control more than \$500 billion in assets, are
5 affiliated with the United Arab Emirates, a country whose human
6 rights record the State Department has described as “problematic”
7 at best, with “significant human rights problems” including
8 arbitrary and incommunicado detention, human trafficking, and
9 “severe restrictions on and abuses of workers’ rights,” among
10 others.

11 (d) Sovereign wealth funds are growing in size and in influence.
12 These funds are already significantly larger than all of the world’s
13 hedge funds combined, and the Chair of the Securities and
14 Exchange Commission has predicted that sovereign wealth funds
15 could grow as large as \$12 trillion by 2015.

16 (e) Public retirement systems in this state currently invest in,
17 and with, private equity firms that are owned in significant part
18 by sovereign wealth funds, including sovereign wealth funds such
19 as those of the United Arab Emirates, that rank among the least
20 transparent and that are funded by governing regimes repeatedly
21 found to have violated basic human rights.

22 (f) These investments face all of the heightened risks described
23 above, and it is unconscionable for this state to invest the retirement
24 funds of its public workers for the benefit of egregious human
25 rights violators.

26 SEC. 2. Section 7513.8 is added to the Government Code, to
27 read:

28 7513.8. (a) As used in this section, the following definitions
29 shall apply:

30 (1) “Board” means the Board of Administration of the Public
31 Employees’ Retirement System or the Teachers’ Retirement Board
32 of the State Teachers’ Retirement System, as applicable.

33 (2) “Company” means a sole proprietorship, organization,
34 association, corporation, partnership, venture, or other entity, and
35 any subsidiary or affiliate, that exists for profitmaking purposes
36 or to otherwise secure economic advantage.

37 (3) “Invest” or “investment” means the purchase, ownership,
38 or control of stock or partnership shares of a company, the
39 commitment of funds or other assets to a company, or the

1 commitment of funds or other assets to be managed or subsequently
2 invested by a company.

3 (4) “Own” or “owned” means the ownership or control of any
4 stock or partnership shares of a company.

5 (5) “Private equity company” means any sole proprietorship,
6 organization, association, corporation, partnership, venture, or
7 other entity, and any subsidiary or affiliate, that, as one among its
8 principal investment strategies, invests in securities that are not,
9 immediately following the company’s investment, listed on a public
10 exchange. For purposes of this section, “private equity company”
11 does not include a company or any subsidiary or affiliate that is
12 itself listed on a public exchange.

13 (6) “Sovereign wealth fund” means a government investment
14 vehicle which is funded by foreign exchange assets, and which
15 manages those assets separately from the official reserves of the
16 relevant country’s monetary authorities.

17 (b) The board shall not make any additional or new investment,
18 or renew any existing investment, in a private equity company that
19 is owned in whole or in part by a sovereign wealth fund, and shall
20 not make any additional or new investment, or renew any existing
21 investment, in a fund managed directly or indirectly by a private
22 equity company that is owned in whole or in part by a sovereign
23 wealth fund, if any country or federation of countries with which
24 the sovereign wealth fund is affiliated, either directly or indirectly,
25 is not a signatory or party, as the term is used by the United
26 Nations, to at least five of the following international treaties listed
27 in this subdivision.

28 (1) The International Covenant on Economic, Social and
29 Cultural Rights.

30 (2) The International Covenant on Civil and Political Rights.

31 (3) The International Convention on the Elimination of All
32 Forms of Racial Discrimination.

33 (4) The Convention on the Elimination of All Forms of
34 Discrimination Against Women.

35 (5) The Convention against Torture and Other Cruel, Inhuman
36 or Degrading Treatment or Punishment.

37 (6) The Convention on the Rights of the Child.

38 (c) The prohibition stated in subdivision (b) shall not apply if
39 either of the following conditions is met:

1 (1) The United States Department of State has determined, in
2 the most recent applicable human rights report prepared pursuant
3 to Section 2151n or 2304 of Title 22 of the United States Code,
4 or the report prepared pursuant to Section 2464 of Title 19 of the
5 United States Code, that the country, countries, or federation of
6 countries with which the sovereign wealth fund is affiliated, either
7 directly or indirectly, generally respects the human rights of its
8 citizens.

9 (2) The United States Department of State did not prepare a
10 human rights report, as described in paragraph (1), for the country,
11 countries, or federation of countries with which the sovereign
12 wealth fund is affiliated, either directly or indirectly, in the most
13 recent year for which these reports were prepared.

14 (d) If the prohibition in subdivision (b) does not apply, the board
15 shall do all of the following before making any additional or new
16 investment, or renewing any existing investment, in a private equity
17 company that is owned in whole or in part by a sovereign wealth
18 fund, and before making any additional or new investment, or
19 renewing any existing investment, in a fund managed directly or
20 indirectly by a private equity company that is owned in whole or
21 in part by a sovereign wealth fund:

22 (1) Evaluate every sovereign wealth fund that owns any stock
23 or shares in the private equity company at issue according to all
24 of the following criteria with respect to which there is publicly
25 available information or information that the board may obtain
26 using its best efforts:

27 (A) Transparency, which shall include consideration of:

28 (i) Whether and the extent to which the sovereign wealth fund
29 publishes an annual report that details its investment activities, the
30 type, nature, size, and geographic location of each of its
31 investments, its returns per investment, and the currency
32 composition of its investments.

33 (ii) Whether and the extent to which the sovereign wealth fund's
34 source of funding is clearly specified, its objective and investment
35 strategy are clearly communicated, the role of the government and
36 of managers in setting the sovereign wealth fund's investment
37 strategy is clearly established, and ethical guidelines and guidelines
38 for corporate responsibility are in place and clearly communicated.

39 (iii) Any additional transparency-related criteria the board, in
40 its discretion, determines to be appropriate.

1 (B) Political stability, which shall include consideration of the
2 record of any country, countries, or federation of countries with
3 which the sovereign wealth fund is affiliated, either directly or
4 indirectly, regarding the following, with a particular focus on
5 subparagraph (ii):

6 (i) Internal and external conflict, public corruption, and
7 procedures for democratic accountability.

8 (ii) Respect for and effective enforcement of internationally
9 recognized human rights, as set forth in the Universal Declaration
10 on Human Rights.

11 (iii) The presence and effective operation of an independent
12 judiciary.

13 (C) Productive labor practices, which shall include consideration
14 of the record of any country, countries, or federation of countries
15 with which the sovereign wealth fund is affiliated, either directly
16 or indirectly, regarding the effective prohibition of child and forced
17 labor, the effective enforcement of rights to organize, to strike,
18 and to bargain collectively, and the effective enforcement of the
19 rights and principles stated in the International Labor
20 Organization's Declaration on Fundamental Principles and Rights
21 at Work.

22 (D) Corporate social responsibility, which shall include
23 consideration of whether the sovereign wealth fund is in
24 compliance with the Global Sullivan Principles of Corporate Social
25 Responsibility and the United Nations' Principles for Responsible
26 Investment.

27 (2) Prepare a detailed written report of the evaluation conducted
28 pursuant to paragraph (1). This report shall be a public record
29 within the meaning of the California Public Records Act (Chapter
30 3.5 (commencing with Section 6250)) and shall not be considered
31 due diligence materials within the meaning of Section 6254.26.
32 The report shall be made publicly available and available on the
33 Internet at least 60 days prior to any final investment decision as
34 described in paragraph (3).

35 (3) Consider the evaluation required by paragraph (1) and the
36 report required by paragraph (2) before making any final
37 investment decision regarding any additional or new investment,
38 or the renewal of any existing investment, in a private equity
39 company that is owned in whole or in part by the sovereign wealth
40 fund subject to the evaluation and report, and before making any

1 final investment decision regarding any additional or new
2 investment, or the renewal of any existing investment, in a fund
3 managed directly or indirectly by a private equity company that
4 is owned in whole or in part by the sovereign wealth fund subject
5 to the evaluation and report.

6 (e) In those cases where the board's evaluation pursuant to
7 paragraph (1) of subdivision (d) reveals evidence of a serious lack
8 of transparency, lack of respect for internationally recognized
9 human rights, lack of productive labor practices, or lack of
10 compliance with the applicable principles for socially responsible
11 investing, the board shall do both of the following:

12 (1) Not make any additional or new investment, or renew any
13 existing investment, in a private equity company that is owned in
14 whole or in part by the sovereign wealth fund subject to the
15 evaluation, and not make any additional or new investment, or
16 renew any existing investment, in a fund managed directly or
17 indirectly by a private equity company that is owned in whole or
18 in part by the sovereign wealth fund subject to the evaluation,
19 unless the board determines that the failure to do so would be
20 inconsistent with its fiduciary responsibilities as described in
21 Section 17 of Article XVI of the California Constitution.

22 (2) State in writing whether it has decided not to make the
23 investment at issue or whether it has decided to proceed with the
24 investment, notwithstanding the evidence described in paragraph
25 (1) of subdivision (d). This statement shall be a public record within
26 the meaning of the California Public Records Act (Chapter 3.5
27 (commencing with Section 6250)) and shall be made publicly
28 available and available on the Internet within 10 days of the board's
29 final investment decision.

30 (f) On or before January 1, 2010, and every year thereafter, the
31 board shall file a report with the Legislature. The report shall
32 describe all of the following:

33 (1) Any decision not to make a new or additional investment,
34 or not to renew an existing investment, that was made as a result
35 of the prohibition in subdivision (b).

36 (2) Any decision to not to make a new or additional investment,
37 or not to renew an existing investment, that was made as a result
38 of the evaluation or report required by paragraphs (1) and (2) of
39 subdivision (d).

(3) Any decision to make a new or additional investment, or to renew an existing investment, that was made notwithstanding evidence of a serious lack of transparency, lack of respect for internationally recognized human rights, lack of productive labor practices, or lack of compliance with the applicable principles for socially responsible investing, and the reasons why the decision was required to ensure consistency with the board's fiduciary responsibilities as described in Section 17 of Article XVI of the California Constitution.

(g) Nothing in this section shall require the board to take any action unless the board determines, in good faith, that the action is consistent with the fiduciary responsibilities of the board as described in Section 17 of Article XVI of the California Constitution.

(h) This section shall be known and may be cited as the Responsible Private Equity Investment Act of 2008.

SEC. 3. Section 16642 of the Government Code is amended to read:

16642. Present, future, and former board members of the Public Employees' Retirement System or the State Teachers' Retirement System, jointly and individually, state officers and employees, research firms described in subdivision (d) of Section 7513.6, and investment managers under contract with the Public Employees' Retirement System or the State Teachers' Retirement System shall be indemnified from the General Fund and held harmless by the State of California from all claims, demands, suits, actions, damages, judgments, costs, charges and expenses, including court costs and attorney's fees, and against all liability, losses, and damages of any nature whatsoever that these present, future, or former board members, officers, employees, research firms as described in subdivision (d) of Section 7513.6, or contract investment managers shall or may at any time sustain by reason of any decision to restrict, reduce, or eliminate investments pursuant to Sections 7513.6 and 7513.7, *or by reason of any evaluation conducted or report made pursuant to Section 7513.8, or by reason of any investment decision made in compliance with Section 7513.8.*

SEC. 4. The provisions of this act are severable. If any provision of this act or its application is held invalid, that invalidity

- 1 shall not affect other provisions or applications that can be given
- 2 effect without the invalid provision or application.

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